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NSW CHILDCARE INSIGHT

MAY 2024

PERFECT STORM FOR LARGE GROWTH IN DAILY CHILDCARE RATES

This Childcare Insight for NSW offers perspective into the multiple market factors that are culminating to drive daily childcare rates higher, creating a flow-on effect into valuations for the sector.

The New South Wales childcare sector is currently experiencing a 'perfect storm' for significant growth in daily childcare rates *(see Figure 1)*, due to multiple factors that are impacting the market.

These market factors include:

- Expected strong growth in demand for childcare places. Labour force participation rates are forecast to trend upwards in most states and territories over the medium to longer-term, which is expected to contribute to a continued increase in the average number of hours children can attend childcare per week. These factors will drive demand for childcare and the development of new childcare centres in some areas.
- The increasing cost of construction in the current inflationary environment, which has driven up rent for new childcare centres. In turn, this has placed upward pressure on daily rates required to secure well-located, quality facilities which are in demand.
- Strong government subsidies continue to influence childcare centre valuations. There is strong bipartisan government support for the childcare sector that will see continued funding towards childcare subsidiary for households. This funding has resulted in continued upward pressure on the average daily rate per child across all states which has grown by $10-20 per day. This is a large increase in discretionary spending for most family households.
- Typical long term lease structure with 'ratchet clauses' across New South Wales has resulted in strong rental growth following rent reviews. This has added to the rental burden on childcare businesses and is translating to growth in daily rates.

MARKET FACTORS ARE DRIVING GROWTH IN DAILY

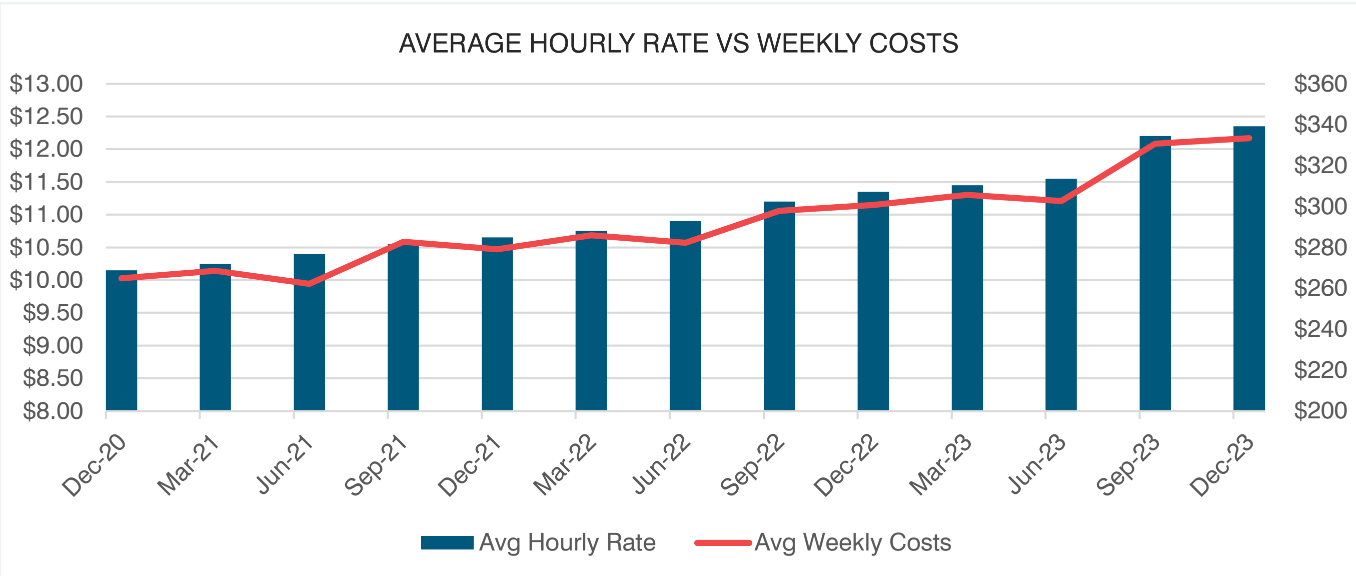


Figure 1 – Source: Oxford Economics

CHILDCARE RATES

Current market factors are culminating to drive up daily rates in the New South Wales childcare sector. Increasing demand for childcare places, along with the rising cost of construction, and the typical lease structures common in the sector, are having a flow-on effect into childcare centre valuations. This is leading to an increase in daily rates.

As construction costs increase, childcare centres need to be able to afford their premises, with well-located, quality facilities the main factors affecting the occupancy and competition between childcare centres. We expect to see more existing centres undergoing refurbishments and upgrades going forward to compete for customers within their catchments.

As these costs grow, they continue to be subsidised heavily by the Government, injecting more capital into the sector, and placing further upward pressure on daily rates.

Operation of childcare centres is expected to become more consolidated as major institutional groups continue acquiring centres and portfolios of centres. We also expect to see further activity from private equity firms over the medium-term.

In tandem with these factors, Government is committed to providing funding towards a wage increase for the early childhood education and care workforce, which is also influencing valuations *(see Figure 2)*.

The Australian Government's investment last year in 'cheaper childcare' saw out-of-pocket costs fall and benefitted more than one million families.

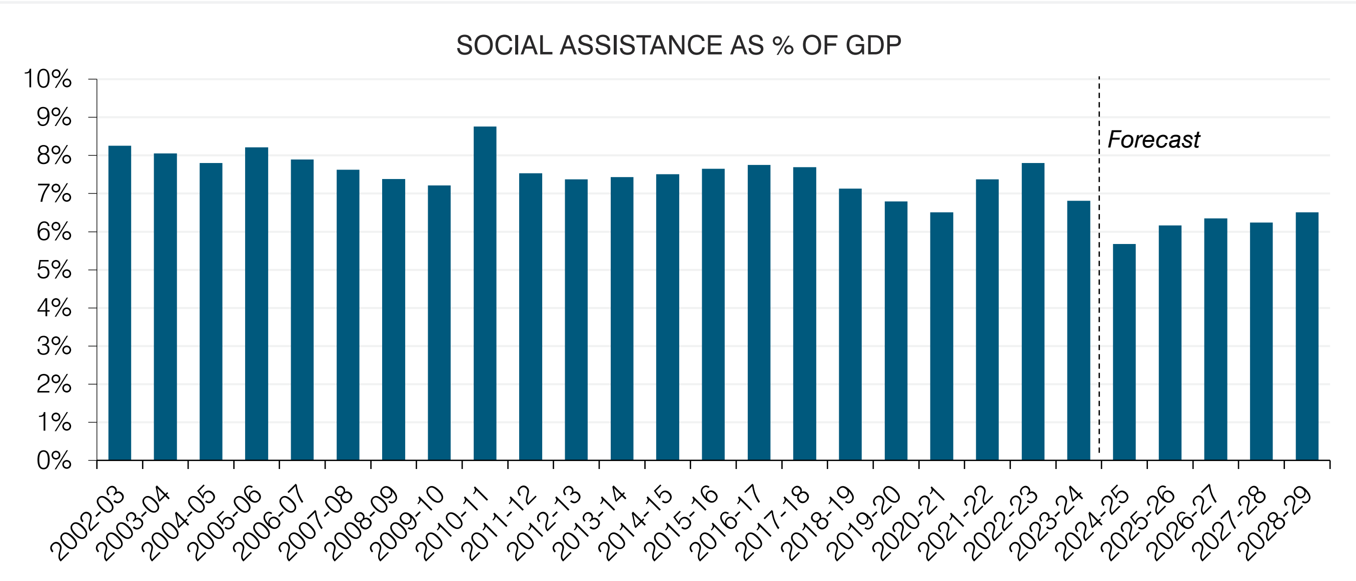


Figure 2 – Source: Oxford Economics

The 2024–25 Budget continues to build on these initiatives, with new measures expected to deliver net savings of $410.7 million over four years from 2024–25 by strengthening the payment and accuracy of the Child Care Subsidy (CCS) program.

While childcare subsidies are translating into an increase in wages for childcare workers, over the longer-term with will translate into higher operational costs and continued upward pressure on daily rates. Moreover, more families will need to pay for their own placements as a result of modifications to the CCS program.

HOW THE ACCC CHILDCARE ENQUIRY IS IMPACTING THE MARKET

In late 2022 it was announced that the ACCC was conducting an inquiry into the supply of childcare services and childcare pricing nationally. The final report was released 29th January 2024, reporting 31 findings and highlighting:

- Current Childcare market is not delivering on accessibility and affordability for all children and households across Australia.
- Governments need to change their “one size fit all” regulations to be able to meet community expectations and meet its objectives.
- Childcare fees have grown faster than inflation and wage growth since the introduction of CCS. *(See Figure 3 - this is the average cost to send one child to childcare per week vs the Real Discretionary spending level).*
- Labour is the main driver of Childcare costs, accounting for 69% of centre-based centre costs and 77% of after-school hour care. Land and related costs are the other significant costs, although much lower in comparison.
- Location and quality are the main factors affecting the occupancy and competition between childcare centres.

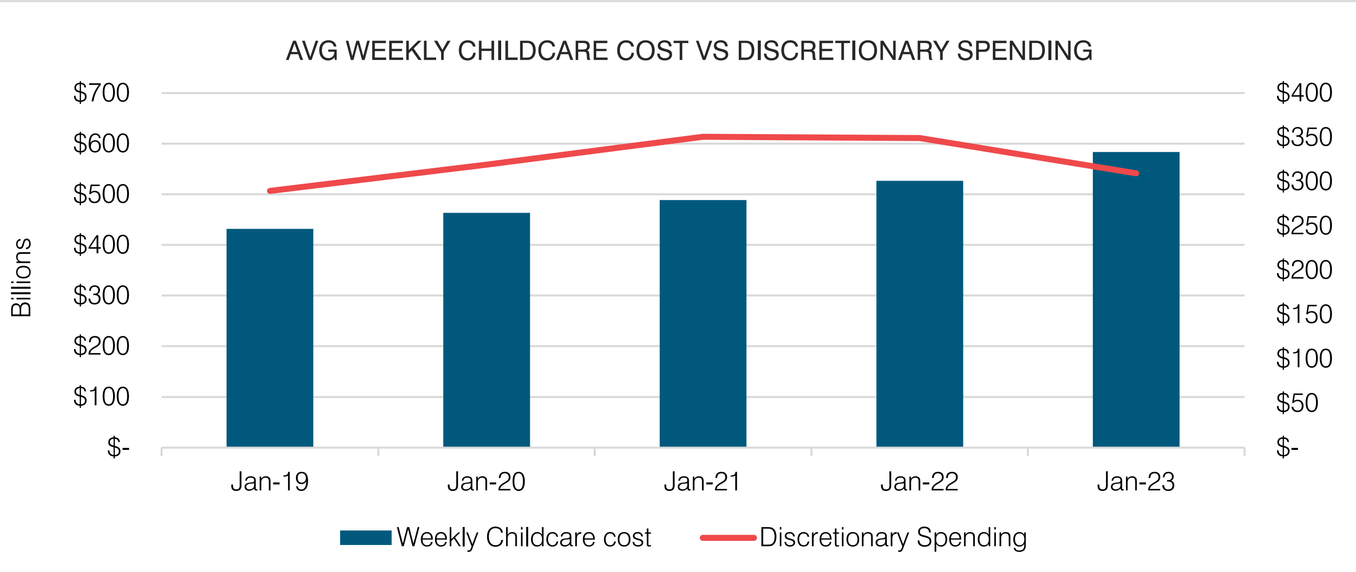


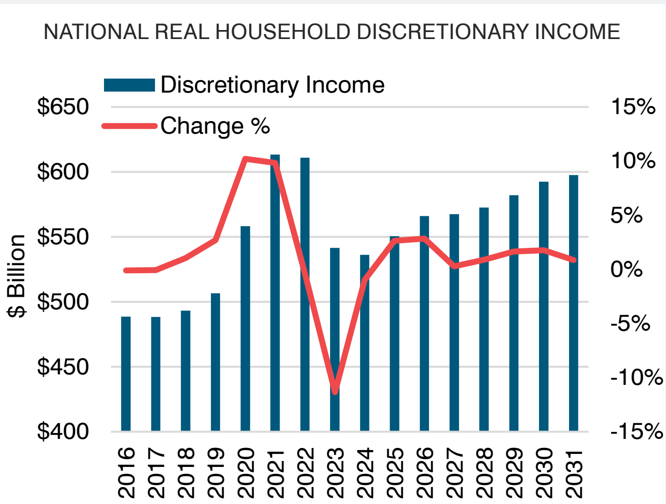
Figure 3 – Source: Department of Education & Oxford Economics

The ACCC put forward eight different recommendations:

- Federal government to reconsider and restate key objectives as a priority for the sector, namely the price regulation mechanism.
- Readjustment of the Childcare Subsidiary system and hourly rate cap.
- Reconsideration of information's and data provided for parents and guardians, namely accurate estimation of out-of-pocket costs, increasing reporting frequency, transparency of critical information etc.
- Retention structure of educators and work force in the childcare sector.
- Policy options for homecare service users.
- Expansion and maintenance of First Nation Children care services and its users.
- Federal, state and territory governments to regulate and monitor the childcare market to deliver the government's objectives, targeting underserved and unserved markets.
- Considerations of benefits and challengers involved with direct market intervention methods.

HOUSEHOLD INCOME GROWTH STALLS

While childcare daily rates are going up, household income growth has stalled with discretionary income reduced by –1% for 2024 and -12.56% since a record high in 2021. This is not expected to increase until 2025 *(see Figure 4)*.



Source: Oxford Economics

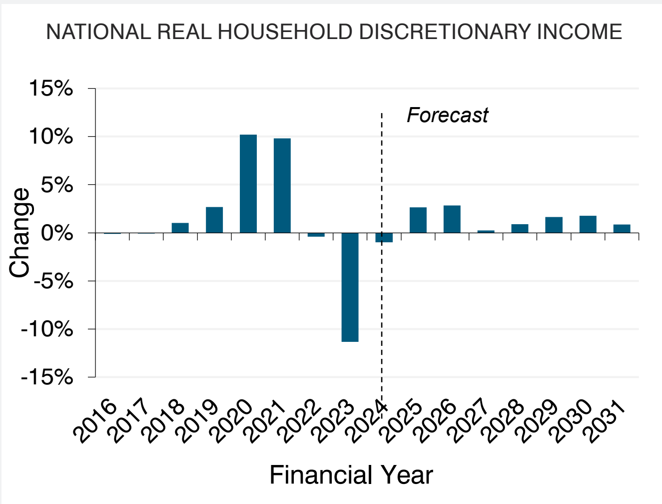


Figure 4 – Source: Oxford Economics

CHILDCARE CENTRE DEMAND VERSUS SUBSIDY PAYMENTS

Over the medium-term, the number of children aged 0 to 5 years is forecast to increase most strongly in Queensland, followed by Victoria and West Australia, with lower but still strong growth expected in all other states and territories.

Furthermore, labour force participation rates are forecast to trend upwards in most states and territories over the medium- to longer-term and this is expected to contribute to a continued increase in the average number of hours children attend childcare per week.

These factors will drive demand for childcare and the development of new childcare centres in some areas.

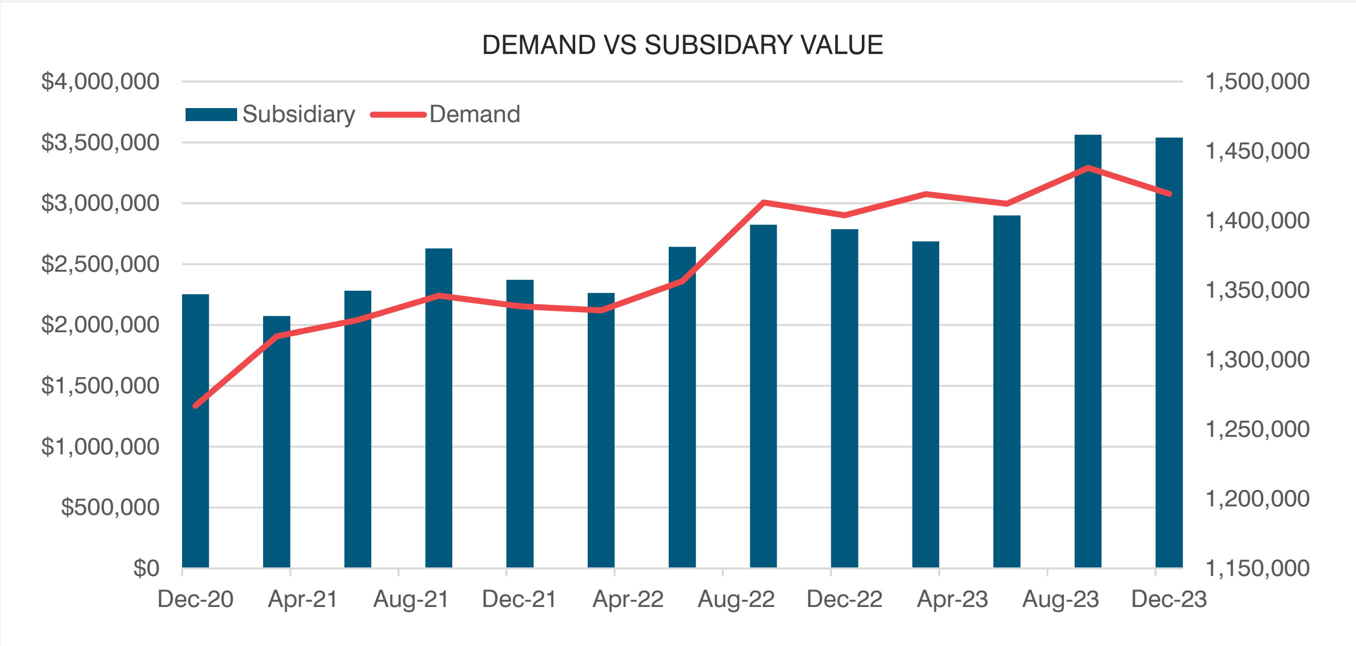


Figure 5 – Source: Oxford Economic

The maximum subsidy amount increased to 90% for one child and 95% for two children from 1 July 2023, and the household income eligibility cap increased to $530,000, making childcare more affordable due to subsidisation. *(See Figure 5 – this graph indicates demand [number of children using childcare services] and subsidiary payments over the quarter period.)*

CHILDCARE COSTS TO BECOME MORE EXPENSIVE FOR PARENTS

While Government subsidies will ensure childcare workers are paid more, childcare costs are likely to become more expensive for parents with modifications to the CCS program.

This may make childcare less affordable for parents in New South Wales while daily childcare rates continue to increase. *(See Figure 6 – Source: Oxford Economic. This is the average cost to send one child to childcare per week vs the weekly income per person, as well as a percentage of childcare fee against income per week).*

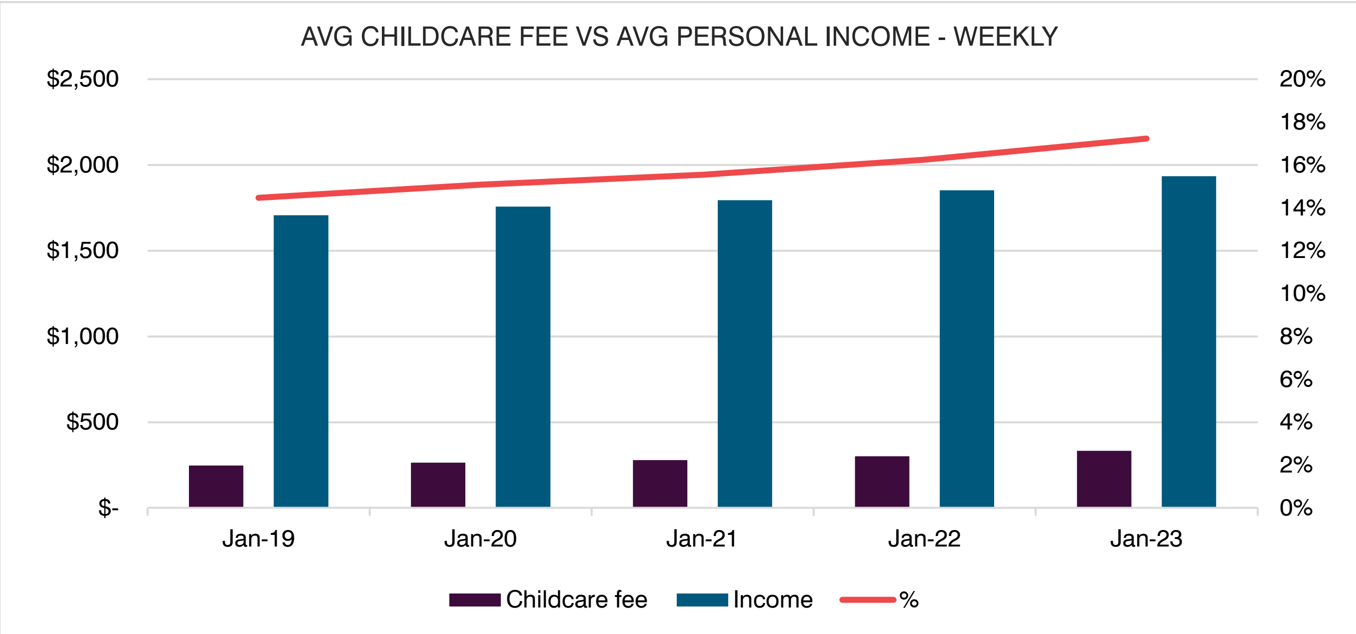


Figure 6 – Source: Oxford Economic

CONTACT THE TEAM

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